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Editor's Note: Environmental issues have become increasingly important to all businesses and individuals. This edition of the Quarterly focuses on several issues—including federal, state and local criminal prosecution and manufacturers' liabilities—of current interest.

State and Local Enforcement

The Criminal of the 1990's— The Polluter

In the 1990's, state and local prosecutors will depart from pursuing only "traditional" criminal activities and, instead, focus on a new type of crime. The victim of this crime is not a person. The victim is the environment. The crime is polluting and the criminal is any business or person (including managers and officers of the business) improperly disposing, transporting, storing, or handling "hazardous waste." Such businesses and persons will be labeled "polluters" by the prosecutor and will face stiff fines and, more importantly, the possibility of going to jail.

The Factors Influencing the Increased Prosecutions

Many factors can be cited to explain the change in the prosecutors' focus away from traditional crimes and toward environmental crimes. Without question, preserving our environment and environmental cleanup are of paramount concern to everyone. There is also a growing discontent with the efficiency of large civil remediation actions against polluters. Civil actions to address environmental damage can take years to resolve, if at all, and (from a prosecutor's perspective) only result in the payment of damages. In contrast and in light of the speedy trial guarantees under the Constitution, a criminal prosecution against a polluter runs a very short course and will typically have a lifespan of months, not years.

A criminal prosecution also presents much more

severe penalties to the polluter—i.e., a felony conviction and jail time. Prosecutors believe that many companies can simply factor the payment of large civil judgments for environmental damage caused by the company into the cost of doing business. But a criminal prosecution, even if no conviction results, cuts to the heart of a company's "good will" and an individual's reputation and standing in the community. Therefore, criminal prosecutions are viewed as an excellent deterrent against polluting.

What is the Crime?

Most criminal actions will be prosecuted by local district attorneys' offices and under the Hazardous Waste Control Act (California Health and Safety Code Section 25100 *et seq.*) (hereinafter "H & S Code"). Most prosecutions will be premised on H & S Code Section 25189.5, which proscribes the illegal transportation or disposal of hazardous waste. Hazardous waste is defined, in part, in the H & S Code as: "A waste . . . which, because of its quantity, concentration, or physical, chemical, or infectious characteristics, may either: (A) Cause, or significantly contribute to, an increase in mortality or an increase in serious irreversible, or incapacitating reversible, illness; or (B) Pose a substantial present or potential hazard to human health or environment when improperly treated, stored, transported, or disposed of, or otherwise managed." (H & S Code Section 25117.)

As with all criminal prosecutions, the prosecutor must prove: (1) an act proscribed by law and (2) some form of an intent to commit the act. The first requirement is met by proving a violation of the provisions of



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Continued on page 5

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Criminal Liability for Corporate Officers and Managers Under Federal Environmental Laws

The Increasing Trend toward Criminal Enforcement

Since its inception in 1982, the United States Department of Justice's ("DOJ") environmental criminal enforcement section has successfully prosecuted 472 criminal enforcement actions under the provisions of federal environmental laws. Three hundred thirty-one of these convictions were of individuals, including corporate officers and managers. The remaining convictions were of the corporate entities themselves. Aggregate penalties resulting from these convictions include over \$28 million in fines and over eight years of jail time.

Criminal enforcement at the federal level is accelerating—over half of the penalties collected were obtained in the past 18 months. The number of federal enforcement personnel has also grown dramatically. From the early days of one attorney for the entire country, DOJ's headquarters section has grown to 25 full-time environmental criminal prosecutors.

In addition to headquarters staff, each local U.S. Attorney's Office has attorneys who prosecute environmental crimes. Moreover, the Federal Bureau of Investigation ("FBI") now has over 150 agents who handle environmental crimes. In addition to DOJ staff, the United States Environmental Protection Agency ("EPA") has 52 special agents from the National Enforcement Investigation Center ("NEIC") who work with each of EPA's 10 Regional Offices to investigate environmental law violations and bring criminal prosecutions. Federal criminal prosecutions are ongoing today in EPA Region 9 which covers California, Arizona, Hawaii, Nevada, and the Pacific Islands.

What does this mean to the businessperson? It means that owners, managers and employees of businesses that produce virtually any type of waste product are subject to criminal prosecution under federal environmental laws for activities that many would consider normal, everyday business activities.

Of overwhelming importance for the businessperson is the fact that almost every violation can be punished, at the discretion of the enforcement agency, as a civil or criminal violation. To obtain a greater impact on the regulated community, federal enforcement agencies are turning to criminal enforcement. A business manager or officer can minimize the threat of falling victim to this new emphasis on criminal enforcement, however, by understanding the laws' requirements and ensuring that they are met in a timely, good-faith manner.

Some statutes require that the violator know of the violation. Under other laws, a criminal conviction can result from mere negligent acts. Prosecution can mean a felony conviction, fines of up to \$1,000,000 per day, jail sentences, business closure, and in certain circumstances, even seizure of the business. Given the high stakes,

every business manager must be aware of the laws and the possible consequences of a violation.

Each of the major federal environmental laws contains criminal provisions. A description of these follows.



Jon K. Wactor

Federal Environmental Criminal Provisions

A. Clean Air Act

The Clean Air Act ("CAA"), which regulates stationary and mobile sources of air contaminants, is one of the earliest of the federal environmental laws. It requires compliance with air emission limits. Criminal penalties of up to \$25,000 per day of violation and up to one year in jail are available under Section 113 of the CAA for *knowing* violations of the law's provisions. Higher penalties are available for repeat violators.

B. Clean Water Act

The Clean Water Act ("CWA"), or Federal Water Pollution Control Act ("FWPCA"), regulates discharges of pollutants or contaminants into "waters of the United States" from a point source. "Waters of the United States" has been construed by the courts to include dry arroyos, storm drain systems, "artificial" waters, wetlands, and so on. "Pollutant" has been defined to include rocks, sand, dredge spoil, soapy water, metals, heat, and most everything else. This law requires a federal permit for every discharge of pollutants into a water of the United States.

Examples of discharges include dredging, grading and filling of wetlands, and the spilling, leaking, or pouring of pollutants into bays, streams, rivers, and their tributaries. Criminal penalties for *negligent* violations such as failure to obtain a permit, violation of permit limits, tampering with monitoring equipment, and so on, include fines of up to \$25,000 per day, plus one year in jail. *Knowing* violations carry fines of up to \$50,000 per day and three years in jail for the first violation. Higher penalties are available for repeat violators.

Continued on page 6

the H & S Code and will typically involve an accusation of the transportation or disposal of hazardous waste without the proper permits. However, criminal culpability can also be premised on:

- Storing hazardous waste for more than 90 days without a proper permit;

- Handling hazardous waste in a manner which causes an unreasonable risk of fire, explosion, serious injury or death (regardless of whether the risk ever materializes); and

- Making any false statement in an application, label, manifest, or record relating to hazardous waste management.

The most common activities which will produce exposure to criminal liability include improper transport or disposal, on-site spills, waste discharge into public sewers, improper storage of drums, and the improper removal of asbestos or other hazardous material from existing buildings.

The second element of the crime, which involves the mental component, is more perplexing. Under traditional concepts of criminal law, mere ordinary negligence is insufficient to convict for a criminal offense. Traditionally, criminal law requires an actual intent or recklessness by a defendant as the necessary mental component of a crime. However, in the context of environmental crimes, the trend is moving toward a strict liability standard—i.e., criminal liability without regard to the defendant's intent. This trend is evidenced by a recent court's holding in *People v. Martin* (1989) 211 Cal.App.3d 699. In *Martin*, the court held that ordinary civil negligence was sufficient to convict a polluter for a criminal violation of H & S Code Section 25189.5 and affirmed a felony conviction against a president of a chemical company. The court reasoned that Section 25189.5 was a "public welfare" offense or a *malum prohibitum* crime. A conviction for a public welfare offense could be premised on strict liability, which requires no proof of fault whatsoever on the part of the defendant. "[I]t follows," said the court, "that it [the Legislature] could instead choose to punish those who reasonably should have known they were transporting or disposing of hazardous waste at or to a nonpermitted facility." (*Martin, supra*, 211 Cal.App.2d at 714.)

In summary, every aspect of hazardous waste management or handling is subject to criminal prosecution.

As a consequence of the *Martin* case, virtually any violation, regardless of the defendant's intent, is subject to a criminal prosecution.

Who Are the Potential Defendants and What is the Punishment?

The potential defendants are any businesses and employees of businesses which deal with hazardous waste. However, prosecutors tend to target larger, more financially solvent businesses because of the ability to pay criminal fines. Prosecutors will also target repeat offenders, any conduct motivated by profits, or conduct found to be egregious, e.g., the midnight dumping of oil drums in the desert. In an effort to deter conduct and "make an example," prosecutors will attempt to climb up the corporate ladder and convict company managers or officers on the basis that these individuals knew or "should have known" about the company's illegal activities.

If convicted, both the company and the individual face large fines. Penalties range from \$5,000 to \$100,000 per violation and up to 36 months of jail time per violation. Therefore, repeated offenses, e.g., repeated spills on site, expose both the company and the individual to increased fines and increased jail time.

How Can Criminal Liability be Avoided or Mitigated?

Potential criminal liability can be avoided or mitigated by three steps. First, a business dealing with hazardous material should conduct an "environmental audit" with the assistance of competent technicians and legal counsel. The audit should be designed to ensure that the practices of the business meet all environmental requirements. Second, employees should be properly informed and trained regarding the handling of hazardous material. Periodic and follow-up instruction should also occur. Third, once a problem is identified, it should be dealt with and not ignored, even if criminal exposure is possible. The purpose of prosecuting an environmental crime is to protect and preserve the environment, not to put people in jail. Accordingly, any remedial measures by the "polluter" may lessen the potential punishment.

For more information regarding this article, contact David Henry Dolkas at (619) 738-7732.

C. Resource Conservation Recovery Act

The Resource Conservation Recovery Act ("RCRA") regulates the generation, storage, transport, import, export, treatment, and disposal of hazardous wastes. RCRA's regulations list certain specific hazardous wastes which are common byproducts of manufacturing, metal plating, leather tanneries, and so on. In addition to specific denominated wastes, RCRA also regulates wastes which have hazardous characteristics including corrosiveness and reactivity.

RCRA requires every facility that handles hazardous wastes to register with the EPA and follow carefully prescribed procedures. Violation of these procedures, which govern every aspect of hazardous waste handling, can result in criminal penalties under RCRA Section 3008. Criminal penalties include fines of up to \$50,000 per day and jail sentences of up to two years for a *knowing* first violation, with increased penalties for subsequent violations. In addition, a penalty of up to \$1,000,000 per day is available for a knowing violation of RCRA while knowingly placing another person in imminent danger of death or serious bodily harm. A 15-year jail sentence is also possible with this violation.

D. Toxic Substances Control Act

The Toxic Substances Control Act ("TSCA") regulates the manufacture, transportation, shipment, import and export of chemical "substances and mixtures" and asbestos. Violation of TSCA can result in a criminal penalty of up to \$25,000 per day and up to one year in prison.

E. Federal Insecticide, Fungicide and Rodenticide Act

The Federal Insecticide, Fungicide, and Rodenticide Act ("FIFRA") regulates the registration, use, transport, import, export and disposal of insecticides, fungicides, and rodenticides. FIFRA Section 136(1) establishes a \$25,000 fine and up to one year in prison for a *knowing* violation of any provision. This penalty may apply to any registrant, commercial applicator, wholesaler, retailer, or other distributor.

F. Comprehensive Environmental Response, Compensation, and Liability Act

The Comprehensive Environmental Response, Compensation, and Liability Act ("CERCLA" or "Superfund") sets up several mechanisms to study and clean up hazardous substances which have, or may, contaminate the environment at abandoned waste disposal facilities and operational industrial facilities.

CERCLA Section 103 contains three notice and record-keeping requirements. Violation of these requirements gives rise to substantial criminal penalties.

First, Section 103 requires any person in charge of a "facility" (defined as anyplace a hazardous substance may come to be located) to notify immediately the National Response Center of a hazardous substance spill at or above the quantity specified in EPA regulations.

Second, Section 103 also requires notice to EPA of any use of an unpermitted treatment, storage or disposal facility.

Third, Section 103 requires the person in charge of a facility to keep records on the name, location, and condition of the facility as well as the identity, characteristics, origin and condition of any hazardous substances contained or deposited in the facility.

Failure to notify, false notification, and destruction of records in violation of these provisions each carries a potential jail term of up to three years for a first offense and up to five years for a subsequent offense, plus fines as set out in Title 18 of the U.S. Code.

In addition to CERCLA Section 103, the 1986 amendments to CERCLA (Superfund Amendments and Reauthorization Act of 1986, or "SARA") require persons who handle substances deemed to be "extremely hazardous" by EPA to follow certain planning and notice procedures. *Knowing and willful* failure to follow these requirements can result in criminal penalties of up to \$25,000 per day and two years' imprisonment for the first offense. Subsequent offenses can result in criminal fines of up to \$50,000 per day of violation and imprisonment for up to five years.

Officer and Management Liability

Managers and officers can be held liable for criminal violations under these laws based upon at least three theories. First, an officer or manager may be held liable based upon his or her personal participation in the act, or by allowing or by directing an employee to conduct the activity. Courts have found managers and officers liable if they were in charge of day-to-day actions of employees or certain activities, even if they had no specific knowledge of certain acts which were illegal. Some courts have gone so far as to hold corporate officers liable even if they had only general responsibility over the corporation's business. Other courts, however, hold that specific knowledge is necessary to obtain a conviction.

Federal prosecutors, who are prosecutors first and environmental attorneys second, tend to rely on their general prosecutorial experience to decide whether to seek a criminal conviction or to proceed with an action for civil penalties. A criminal prosecution is more likely where the prosecutor perceives that the officer, manager or entity has been a "bad actor."

In other words, a criminal charge will probably be

Continued on page 7

avored over a civil action when one or more of the additional criminal elements exists in a case: falsification, long-standing non-compliance, large environmental harm, harm or possible harm to people, economic savings from non-compliance, or destruction of evidence. That list is not all-inclusive but gives a flavor of the factors that may tip the scales toward a criminal charge.

To minimize the chances of a criminal prosecution, managers and officers can perform a management audit to streamline communication channels and to assure proper high-level consideration of the environmental law consequences of business practices. If the managers are aware of the legal requirements and plan to meet them rather than reacting to them during a

time of crisis, the chances of criminal prosecution should be minimized by weeding out the "bad" elements of conduct that can lead to a criminal charge.

For more information on all aspects of environmental law, contact Jon K. Wactor at (619) 699-3691.

Gray Cary's Environmental Law Group provides knowledgeable information and advice on environmental matters to ensure compliance with laws and regulations as part of an overall business strategy. For more information on our environmental services, call David Dolkas, Jon Wactor or Group Chairman John Lormon at (619) 699-3695.

university—and in addition give the grandchild \$10,000 annually without incurring any gift tax.

In what form should the gift be made? Obviously the simplest and most straightforward is by outright transfer. However, particularly in the case of minor beneficiaries, an outright transfer may not be appropriate. The

transfer of property for the benefit of a minor through the California Uniform Transfers to Minors Act is one solution. Here, another trap awaits if we are concerned about estate tax savings. If the donor is also the custodian for the minor under the Uniform Transfers to Minors Act, while the gift is considered complete and the income earned on the property is taxed to the minor, the property will be included in the donor's estate for estate tax purposes if the donor dies while acting as custodian. If a major gift program is anticipated for a minor, the use of an irrevocable trust as the appropriate holding vehicle should be explored. Through such a trust, the \$10,000 annual exclusion can be preserved, and the property can be managed in an effective fashion for the benefit of the minor.

For all gifts, no change in the cost basis of the property for income tax purposes is made. For example, if a stock having a current value of \$9,000 and a cost basis of \$3,000 is transferred to a child, and if the child then sells the stock for \$9,000, the child must report a \$6,000 capital gain on his or her income tax

return for the year in which the property is sold. Because the assets of a deceased person receive a new basis equal to the fair market value of the property at death, the choice of assets for gifts can be an important one. If two stocks are equal candidates for gifts, one with a low cost basis and the other with no built-in gain, then this factor would suggest that the asset with little or no gain be used for the gift. On the other hand, if it is expected that an asset will appreciate in value during the donor's remaining lifetime, the donor may be well advised to get the "future appreciation" of the asset out of his or her estate by a present gift.

While a gift program utilizing the annual exclusion can transfer considerable value from one's estate, we cannot lose track of the most important considerations: both before and after the gift, the donor must feel secure and comfortable with respect to the resources remaining for his or her support and benefit. In addition, the donor must feel comfortable in increasing the total holdings of the individual to whom the gift is made. While there are some traps and many considerations to explore, under present law this remains an excellent tax planning opportunity.

For more information on gift taxes and other trusts and estates matters, contact William E. Beamer at (619) 699-2699.